

University of Mississippi eGrove

Statements of Position

American Institute of Certified Public Accountants
(AICPA) Historical Collection

1978

Proposed statement of position on confirmation of insurance policies in force : audits of stock life insurance companies; Confirmation of insurance policies in force : audits of stock life insurance companies Audits of stock life insurance companies; Exposure draft (American Institute of Certified Public Accountants), 1978, Apr. 5

American Institute of Certified Public Accountants. Auditing Standards Division

Follow this and additional works at: https://egrove.olemiss.edu/aicpa_sop

Part of the [Accounting Commons](#), and the [Taxation Commons](#)

Recommended Citation

American Institute of Certified Public Accountants. Auditing Standards Division, "Proposed statement of position on confirmation of insurance policies in force : audits of stock life insurance companies; Confirmation of insurance policies in force : audits of stock life insurance companies Audits of stock life insurance companies; Exposure draft (American Institute of Certified Public Accountants), 1978, Apr. 5" (1978). *Statements of Position*. 395.
https://egrove.olemiss.edu/aicpa_sop/395

This Book is brought to you for free and open access by the American Institute of Certified Public Accountants (AICPA) Historical Collection at eGrove. It has been accepted for inclusion in Statements of Position by an authorized administrator of eGrove. For more information, please contact egrove@olemiss.edu.

EXPOSURE DRAFT

PROPOSED STATEMENT OF POSITION
ON
CONFIRMATION OF INSURANCE
POLICIES IN FORCE

AUDITS OF STOCK LIFE INSURANCE COMPANIES

APRIL 5, 1978

Issued by the Insurance Companies Committee of the
American Institute of Certified Public Accountants
For Comment From Persons Interested in Auditing and Reporting

Comments should be received by June 5, 1978, and addressed to:
David V. Roscetti, File Ref. No. 3100
AICPA, 1211 Avenue of the Americas, New York, N.Y. 10036



American Institute of Certified Public Accountants

1211 Avenue of the Americas, New York, N.Y. 10036 (212) 575-6200

April 5, 1978

To Practice Offices of CPA Firms; Members
of Council; Technical Committee Chairmen;
State Society and Chapter Presidents,
Directors and Committee Chairmen; Organizations
Concerned With Regulatory, Supervisory, or
Other Public Disclosure of Financial
Activities; Persons Who Have Requested Copies:

An exposure draft of a proposed Statement of Position on "Confirmation of Insurance Policies in Force" accompanies this letter.

In February 1975, the AICPA Special Committee on Equity Funding recommended that the Institute's Auditing Standards Executive Committee consider whether the industry audit guide, Audits of Stock Life Insurance Companies, requires clarification with regard to the confirmation of policies with policyholders. The purpose of this Statement of Position is to identify those circumstances where the independent auditor ordinarily should confirm insurance policies in force.

Comments and suggestions on any aspect of the enclosed draft are sought and will be appreciated. They should be addressed to: David V. Roscetti, File Ref. No. 3100, at the AICPA in time to be received by June 5, 1978. The Insurance Companies Committee will be particularly interested in the reasoning underlying comments and suggestions.

Sincerely,

A handwritten signature in cursive script, reading "John E. Hart".

John E. Hart, Chairman
Insurance Companies Committee

A handwritten signature in cursive script, reading "Thomas P. Kelley".

Thomas P. Kelley, Director
Auditing Standards Division

PROPOSED STATEMENT OF POSITION ON CONFIRMATION OF INSURANCE POLICIES IN FORCE

1. In February 1975, the AICPA Special Committee on Equity Funding stated "... except for certain observations relating to confirmation of insurance in force and auditing related party transactions, generally accepted auditing standards are adequate and ... no changes are called for in the procedures commonly used by auditors." The AICPA industry audit guide, *Audits of Stock Life Insurance Companies* (page 32), states: "It may also be appropriate to select in-force policies for confirmation directly with policyholders of premium amounts, date to which premiums are paid, policy loans, accumulated dividends, etc." The Special Committee recommended "that the Institute's auditing standards executive committee consider whether the Life Insurance Audit Guide requires clarification with regard to the confirmation of policies with policyholders."

2. The Special Committee further stated:

Another auditing procedure, which heretofore has not been considered particularly useful, is verification of the authenticity of a selected number of policies included in the in force inventory by direct confirmation with the policyholders. Such procedure has not generally been considered necessary because it would be unusual for companies to overstate liabilities. Inflation of the inventory of life insurance in force by a company that follows statutory accounting would result in an overstatement of the liability for future policyholder benefits and a reduction in current earnings. However, when companies report on the basis of generally accepted accounting principles (GAAP) there could be

motivation for overstating insurance in force because it could result in an addition to current earnings.

There could be an additional motivation for overstating insurance in force when reinsurance of policies has the effect of materially increasing current earnings, which can occur when a company reports on the basis of either GAAP or statutory accounting. Reinsurance of life insurance policies permits the elimination of the related liability for future policyholder benefits. Under certain circumstances, reinsurance may also result in increasing current earnings to the extent that the proceeds received from reinsurance exceed expenses incurred in connection with the sale and servicing of the reinsured policies.

3. As stated above, the audit guide suggests confirmation of insurance policies in force directly with policyholders; however, the audit guide does not discuss circumstances when confirmation would be appropriate and, as a result, practice has varied. The purpose of this Statement of Position is to identify those circumstances in which the independent auditor ordinarily should confirm insurance policies in force. This Statement of Position is applicable to both stock and mutual life insurance companies.

4. Satisfactory results of the comparison of insurance policies in force with premium collections along with other ordinary auditing procedures (see pages 31-34, 46-47, and 96 of the audit guide) will normally provide the auditor with sufficient competent evidential matter as to the validity of those policies included in the inventory of insurance policies in force. How-

ever, the auditor ordinarily should confirm insurance policies in force with policyholders in the following circumstances:

- a. Proper maintenance of the inventory of insurance in force may be materially deficient due to an absence of segregation of duties or other controls.
- b. Trend analyses or ratios that measure insurance in force indicate erratic or unusual results that have not been satisfactorily explained.
- c. Additions to insurance in force cannot be related to the collection of premiums.
- d. Significant amounts of insurance in force result from related party transactions, and the related party's financial statements are not examined by the auditor.
- e. The company markets insurance products, such as those with immediate cash value features or with unusual commissions arrangements, that could motivate the agent to submit fictitious policies.
- f. Ceded reinsurance activities can materially increase earnings or investable funds.

Effective Date

5. This Statement of Position provides for practices that may differ in certain respects from practices heretofore considered acceptable. Accordingly, this Statement of Position will be effective for examinations made in accordance with generally accepted auditing standards for periods ending on or after December 31, 1978.